

REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON KHAI-MA LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Khai-Ma Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information and actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Khai-Ma Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material impairments

8. As disclosed in notes 29 and 36 to the financial statements, material impairments to the amount of R18 909 000 were incurred as a result of impairment recognised on land and buildings, receivables from exchange as well as receivables from non-exchange transactions.

Material underspending of the budget

9. As disclosed in note 42.3 to the annual financial statements, the municipality materially underspent the operational budget on economic development and the capital budget on corporate services and infrastructure development to the amount of R23 872 209.

Restatement of corresponding figures

10. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of an error discovered during 2014 in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Additional matters

11. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary information

12. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

13. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

14. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

15. The annual performance report was not presented for auditing and, consequently, my findings below are limited to the procedures performed on the strategic planning and performance management documents for the following selected objectives:

- Objective x : Quality living environment – pages x to x
- Objective x : Good governance – pages x to x

16. I assessed the information to determine whether the performance indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (National Treasury's FMPPI).

17. The material findings in respect of all the selected objectives are as follows:

Usefulness of performance information

18. The National Treasury's FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.
- Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
- The period or deadline for delivery of targets must be specified. A total of 100% of the targets were not time bound.
- Performance indicators and measures must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
- Performance indicator and measures must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator and measure. A total of 100% of the indicators/measures were not verifiable.

This was because management did not adhere to the requirements of the National Treasury's FMPPI due to a lack of proper systems and staff constraints.

Compliance with legislation

19. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA are as follows:

Strategic planning and performance management

20. The local community was not consulted by means of a municipal wide structure for community participation in drafting and implementing the integrated development plan, as required by section 28 of the Municipal Systems Act (MSA), 2000 (Act No. 32 of 2000) and regulation 15(1)(a)(i) of the *Municipal planning and performance management regulations*.
21. The municipality did not give effect to its integrated development plan and conduct its affairs in a manner which was consistent with this plan, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and regulation 6 of the *Municipal planning and performance management regulations*.

22. The integrated development plan was not annually reviewed based on the assessment of its performance measurements or changing circumstances, as required by section 34 of the MSA and regulations 3 and 11 of the *Municipal planning and performance management regulations*.
23. The municipality did not establish a performance management system, as required by section 38(a) of the MSA.
24. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the integrated development plan, as required by section 41(1)(a) of the MSA and regulations 1 and 9(1)(a) of the *Municipal planning and performance management regulations*.
25. Measurable performance targets for the financial year with regard to each of the development priorities or objectives and key performance indicators were not set in the integrated development plan, as required by section 41(1)(b) of the MSA and regulation 12(1) and 12(2)(e) of the *Municipal planning and performance management regulations*.
26. The performance of the municipality was not assessed during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA.
27. The annual performance report for the financial year under review was not prepared, as required by section 46 of the MSA and section 121(3)(c) of the MFMA.
28. The annual performance agreements for the municipal manager and all senior managers were not linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan, as required in terms of section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the MSA.

Budgets

29. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

Annual financial statements, performance and annual reports

30. The financial statements submitted for auditing were not prepared, in all material respects, in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, revenue and expenditure identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

Audit committee

31. An audit committee was not in place, as required by section 166(1) of the MFMA.
32. A performance audit committee was not in place, as required by regulation 14(2)(a) of the *Municipal planning and performance management regulations*.

Internal audit unit

33. An internal audit unit was not established, as required by section 165(1) of the MFMA.

Procurement and contract management

34. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by supply chain management (SCM) regulation 17(a) and (c).

35. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
36. Bid adjudication was not always done by committees which were composed in accordance with SCM regulation 29(2).
37. The preference point system was not applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM regulation 28(1)(a).
38. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.
39. The municipality did not implement a supply chain management policy as required by section 111 of the MFMA.
40. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.

Human resources management and compensation

41. An acting municipal manager was appointed for a period of more than three months without the approval by the member of the executive committee for local government, in contravention of section 54A(2A) of the MSA.
42. The municipality did not develop and adopt appropriate policies and procedures to monitor, measure and evaluate performance of staff, in contravention of MSA section 67(d).
43. The acting municipal manager and senior manager directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) MSA.

Expenditure management

44. Reasonable steps were not taken to prevent unauthorised expenditure, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Conditional grants received

45. Municipal systems improvement grant funds were retained or rolled over to the next financial year without seeking the approval of the National Treasury, as required by section 21(1) of DoRA.

Revenue management

46. A credit control and debt-collection policy was not maintained and implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.

Consequence management

47. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

Internal control

48. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

Leadership

49. The mayor did not develop and submit for adoption by the council, a performance management system to report on service delivery. The leadership did not hold staff of the municipality accountable for repeat findings on performance information and compliance with laws and regulations.
50. The position of municipal manager was held by a number of individuals, most of who served in an acting capacity, resulting in a lack of continuity in leadership. A high vacancy rate was experienced in management which negatively impacted on monitoring and oversight. This also led to management not responding in time to audit findings.
51. The leadership did not take timeous and adequate action to address weaknesses at the finance and supply chain management directorates, which resulted in non-compliance with applicable legislation and gave rise to unauthorised, irregular as well as fruitless and wasteful expenditure.
52. The leadership developed an action plan to address audit findings, but adherence to the plan is not monitored on a timely basis.
53. The leadership did not ensure adherence to supply chain management policy at the municipality. This resulted in processes not preventing and, in certain instances, not detecting irregular expenditure and material non-compliance.

Financial and performance management

54. Management did not ensure that all transactions and records were internally checked to detect and correct errors in the financial records throughout the year. This lead to material adjustments in the financial statements at year-end.
55. The accounting officer did not regularly review and monitor management's compliance with all laws and regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted that could have been prevented.
56. The municipality did not have a delegated employee to review and monitor compliance with applicable laws and regulations. There were deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations and performance information.
57. Management did not follow up on the previous audit findings, which resulted in the municipality not submitting an annual performance report for the current and previous financial years.
58. Records management and maintenance disciplines should be refined and included in the daily key controls and reviewed as well as monitored by the appropriate level of management.

Governance

59. Management did not review or monitor risks identified. In addition, no risk assessment was performed relating to the information technology environment.
60. Management did not address previous year findings as the internal audit unit was not established and audit committee was also not established in the current financial year.

Auditor general
Kimberley

30 November 2014



AUDITOR - GENERAL
SOUTH AFRICA

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